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EX PARTE OR **LATE** FILED

November 5,2001

Ms. Magalie Roman Salas
Secretary
Federal Communications Commission
Room TW-B204
445 12th Street, S.W.
Washington, D.C. 20554

Re: CC Docket No. 01-92, Developing a Unified Intercarrier Compensation Regime

Dear Ms. Salas:

Enclosed please find the Reply Comments of the Maryland Office of People's Counsel in the above-referenced docket. I have enclosed four (4) copies pursuant to the Commission's Comment Filing Procedures. Additionally, Comments have been sent to parties on the attached service list and **a** diskette has been submitted.

I have also enclosed an additional copy for receipt-stamp which I ask that you return to me in the enclosed postage-paid envelope.

Should you have any questions regarding this matter, please do not hesitate to contact me.

Very truly yours,

Michael J. Travieso
People's Counsel
Maryland Office of People's Counsel

MJT:sd
Enclosures

Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, D.C. 20554

In the matter of	)	
	)	
Developing a Unified Intercarrier Compensation Regime	)	CC Docket No. 01-92
	)	

REPLY COMMENTS OF THE MARYLAND OFFICE OF THE PEOPLE'S COUNSEL

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Respectfully Submitted **By:**
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November 5, 2001

SUMMARY

I. The unbalanced bill-and-keep proposals are intended to harm the Internet

A. The goal of these proposals is to increase the cost of Internet service. Make no mistake about it, the intentional goal of these proposals is to increase the charges to the Internet. Both the DeGraba and Atkinson-Barnekov documents talk at length about the problems the Internet has caused these FCC Staff members. The FCC Staff proposals are intentionally designed to raise the cost of Internet service by charging customers to "receive" traffic. The Staff members know that the ISPs receive huge amounts of traffic, while originating little or no traffic. Therefore, the proposal to charge for "receiving" traffic are clearly intended to, and would have the effect of, increasing the cost of Internet service. American OnLine (AOL) clearly indicates that ISPs would have to recover from the end users the increase in costs that these price structures would impose on the ISPs. **AOL** correctly states these prices increases for Internet services would harm the demand for Internet services.

B. Harming the Internet is not in the public interest, and is contradictory to the "policy of the United States" to promote the development of the Internet, as stated in Section 230(B) of TA96, as well as the FCC's previously stated goal to facilitate the growth of the Internet.

II. The unbalanced bill-and-keep proposals increase customer rates, thereby harming universal service.

A. Sprint states that if unbalanced bill-and-keep is adopted, Tier 1 LEC end-user rates will increase between $4.00 and $5.00 per line per month. NECA states that the LECs in the NECA Common Line Pool would have to raise end user rates by an average of about $20.00 per line per month if an unbalanced bill-and-keep price structure is implemented in the interstate and intrastate jurisdictions. NECA points out that for those LECs with less than 1,000 lines, the end-user impact of these bill-and-keep proposals would be rate increases between $46.00 and $69.00 per line, per month.

B. Even Qwest, who supports unbalanced bill-and-keep, admits that the "inevitable consequence" of such a proposal is an increase in end-user rates.

C. NARUC's Comments point out the IXCs' historical track record of failing to pass through the benefit of access charge reductions to end-users. NARUC indicates that a failure to pass through access charge reductions to end-users under unbalanced bill-and-keep would result in a rate increase on all consumers.

D. Both NARUC and State Commissions have recognized that the unbalanced bill-and-keep structure would make service unaffordable for many customers.

III. Under the unbalanced bill-and-keep proposals, the effective rate for the surplus traffic is zero.

A. CompTel correctly states that "where the traffic flow" between carriers is "not roughly equal, mandatory bill-and-keep effectively sets an intercarrier compensation rate of zero for the surplus traffic." CompTel also correctly states that "an intercarrier compensation rate of zero is not cost based", and therefore violates numerous regulatory and legal requirements.

B. The fact that unbalanced bill-and-keep inherently has a "zero" rate for the surplus traffic, creates a number of problems, including (a) the "zero" rate service must be subsidized. This creates implicit subsidies. (b) In order to subsidize the free service, the rates for other services must be increased. (c) Giving aware free service to certain customer classifications, whereas that service is not free to other customer classifications, creates a huge incentive for arbitrage.

C. Some parties, including Qwest, SBC, and BellSouth, propose minor adjustments to the unbalanced bill-and-keep proposals. However, no "fine tuning" can correct the inherent flaw in unbalanced bill-and-keep, which is that the surplus traffic has an effective price of zero, and therefore requires subsidy, higher rates for other customers, and attracts arbitrage.

IV. Collecting traffic sensitive costs in a flat rate forces low users to subsidize high users.

A. CompTel correctly indicated that using a flat rate charge to collect the traffic sensitive costs would have the negative effect of taking away consumers' ability to limit toll calling in an effort to keep telephone rates affordable.

B. The effective result of collecting traffic sensitive costs in a fixed, flat monthly rate would be to increase end-user rates so that low use customers would be forced to subsidize high use customers. This is not in the public interest.

CompTel indicated that the imposition of a mandatory bill-and-keep regime where the traffic flow between competing carriers is not roughly balanced would be anti-consumer because under a per-call or per-minute structure, receiving customers could not avoid additional charges unless they refused to answer their phones and refused to use answering machines. Under a flat-rate structure, the called customer would have no means whatsoever to avoid the additional costs, End user customers would be billed the additional, flat monthly charge, even if that customer chose not to answer their telephone at all, and did not receive any calls at all.

C. Requiring customers to pay for receiving unwanted telemarketing calls would be exactly the same as requiring them to pay for receiving unwanted junk mail. Allegiance Telecom's Comments are correct when they state that the DeGraba and Atkinson-Barnekov proposals, which would charge customers to receive calls, make no more sense than if the post office charged customers to receive junk mail. Under the DeGraba, Atkinson-Barnekov, **SBC** and other similar unbalanced bill-and-keep proposals, the price presented to the calling party does not reflect the full cost of the call. Therefore , inefficiency would directly result from changing from a CPNP structure to an unbalanced bill-and-keep price structure. Both CompTel and AT&T also stressed the unreasonableness of charging customers for unwanted calls such as telemarketing calls.

D. AT&T properly recognized that bill-and-keep would not only "subsidize unwanted calls", but would also promote an increase in unwanted calls, since the calling telemarketer would shift part of the costs of every call to the called party, allowing the telemarketers to terminate calls for free.

E. Both WorldCom and CompTel correctly state that the imposition of bill-and-keep where traffic between carriers is not roughly equal will result in a subsidization of services.

V. Unbalanced bill-and-keep provides free service to certain types of "customers," thereby inviting arbitrage.

A. Unbalanced bill-and-keep would create new incentives for arbitrage. Verizon's Comments accurately point out that under unbalanced bill-and-keep, customers that are classified as "carriers" do not have to pay for certain types of transport, while customers who are classified as "end users" do. They state this would cause some end users to try to "masquerade as carriers to try to get the benefit of the better deal."

B. Some ISPs have taken advantage of the existing price structure, by moving to a "carrier" classification in order to charge other carriers very high terminating access charges. However, arbitrage incentives will also arise when a price structure presents the opportunity for certain classes of customers to obtain valuable services for free. This new arbitrage incentive would result under an unbalanced bill-and-keep price structure. Under unbalanced bill-and-keep, a customer can obtain free service by changing their classification from "end-user" to "carrier" (or working with an existing "carrier").

AT&T's Comments correctly recognize that the problem of regulatory arbitrage stems directly from inappropriate rate levels. Therefore, the answer to the problem of arbitrage is to simply ensure that rate levels are appropriate. Giving service away free to certain customer classes does not eliminate arbitrage, it

attracts it. AT&T properly recognizes that unbalanced bill-and-keep creates an arbitrage opportunity to receive valuable services for free.

C. SBC, Qwest, and BellSouth claim that unbalanced bill-and-keep will prevent regulatory "arbitrage". However, it will not prevent it, it will create it. All of the unbalanced bill-and-keep proposals provide free service to customers that are considered "carriers." However, customers that are considered "end users" would pay for similar service. For example, under the SBC proposal, customers that are considered "end users" would pay for both the incoming and outgoing use of the LEC's end office switch to which they are connected. However, under SBC's proposal, by converting from an "end user" to a "carrier" classification, the customer would pay zero for the "incoming" usage of the LEC's switch. In addition, a customer that is considered an "end user" would have to pay for all of the loops connecting between that customer's premise and the LEC's local switch, including the loops that carry incoming and/or outgoing traffic. However, if that end user changed their classification to being a "carrier", then the facilities from the LEC's switch to that customer for incoming traffic would be free.

VI. These proposals would fragment the responsibility for each call.

A. The bill-and-keep proposals would divide the responsibility for each call among three carriers. AT&T's Comments accurately describe the customer's nightmarish task of having to add up the charges of three separate carriers' bills in an attempt to determine what they were paying for their long distance calls, due to the fragmented responsibility under a bill-and-keep price structure. Currently one company is responsible for each call from end-to-end. However, under a bill-and-keep rate structure, no company would have end-to-end responsibility. Under these proposals, three different carriers (originating LEC, IXC, and terminating LEC) would each charge separately for, and have separate responsibility for, different sections of the same call.

B. Due to the fragmented responsibility for calls under bill-and-keep, it would be virtually impossible for the end user to determine which of the several carriers involved in the call was responsible for any quality of service problem. CPE and inside wiring could be separated from the rest of the network for regulatory purposes only because the end user could identify the source of a service problem by physically disconnecting the CPE or inside wiring at the jack or NID. There is no way the end user can separate the three carriers at the "POP" or central office. Therefore, there would be no way for the end user to determine which carrier was responsible for service problems under these bill-and-keep proposals.

VII. The incumbent LECs would still have monopoly power. Unbalanced bill-and-keep would increase the need for regulation.

A. AT&T correctly states that unbalanced bill-and-keep will not limit incumbent LECs' market power, but will rather simply shift the potential for monopoly abuse away from carriers and onto end users. As AT&T correctly quoted:

> Incumbent LECs retain substantial market power, and thus, all that B&K would do is change the entity that must be protected from LEC market power.

For most customers, there is only one company that has a loop to the premise. As a practical matter, the company that has that loop has a "defacto" monopoly on access service to and from the premises. That monopoly power will still exist regardless of whether the DeGraba, Atkinson-Barnekov, or some other unbalanced bill-and-keep proposal is adopted.

B. Unbalanced bill-and-keep would place additional regulatory burdens on the regulators. Regulators would become responsible for identifying and regulating the demarcation points between the different carriers. SBC favors unbalanced bill-and-keep, but even it admitted that bill-and-keep "could encourage inefficient interconnection arrangements, to the extent an IXC could consolidate and relocate its POP only for originating traffic in order to minimize its own transport costs."

C. In addition, SBC states that if bill-and-keep is adopted, many major decisions that the Commission has made with respect to wholesale discounts, universal service, UNEs, and interconnection, and other matters in recent years would have to be discarded and redone.

D. SBC and BellSouth argue that unbalanced bill-and-keep should be adopted in both the state and interstate jurisdictions. What SBC and BellSouth effectively propose is to have the FCC attempt to interfere with the state commissions' jurisdiction over intrastate rates. WorldCom's Comments properly state that the Commission does not have jurisdictional authority to reduce the intrastate switched access rates of carriers. In addition, the FCC Should not require unbalanced bill-and-keep in the intrastate jurisdictions, even if it did have authority to do so, because unbalanced bill-and-keep requires the provision of free service to selected customer classes, which requires implicit subsidies, and creates arbitrage.

VIII. A customer should not have to pay for receiving calls, just because the LEC printed their telephone number in the directory.

A. Sprint argues that by making his or her telephone number available in the white pages directory, a customer is indicating a willingness to receive telephone calls. Sprint argues this demonstrates that called party plays a role in causing the

cost of a call. However, customers do not place their names in the white pages, the LEC does. In most states, the LEC will print the customers' names in the directory, even if a customer asks them not to, unless the customer pays the LEC a separate monthly "non-published" rate to prevent the LEC from publishing their telephone number.

In addition, if wireline customers were forced to pay to receive calls, then it is reasonable to expect that the wireline telephone books would either disappear or have greatly reduced listings, which is similar to what currently exists for wireless services. Wireless customers frequently must pay for received calls. Therefore, they generally do not want their wireless telephone number listed in directories. This would devalue the network.

B. CompTel recognizes that bill-and-keep would create the perverse result of customers being forced to pay for unwanted calls, which would likely lead to customers refusing to answer their phones and answering machines. This is supported by what has happened in the cellular industry, where cellular customers turn their phones off when not placing calls, since they are generally charged to receive calls.

C. Qwest argues that it is acceptable to charge customers to receive calls because the called party "chooses whether to accept the call". However, Qwest's argument is flawed. The proponents of bill-and-keep generally support the imposition of a flat rate charge on end users to pay for the traffic sensitive costs of receiving calls. Therefore, the customers would be charged for receiving calls, regardless of whether a specific customer chose to answer or not answer their telephone.

D. Qwest argues that bill-and-keep is efficient because "it gives called parties appropriate incentives to end calls earlier if their continuation would be inefficient". However, bill-and-keep actually creates inefficiency: bill-and-keep charges the recipient of a call, despite the fact that the originator is the only one in a position to make an efficient decision, because the originator is the only one who knows the content and value of the call. Even if a customer quickly hangs up after realizing that "continuation would be inefficient", the most expensive traffic sensitive parts of a call have already been incurred to "setup" the call.

IX. Unbalanced bill-and-keep does not eliminate the need to recover common costs.

A. Unbalanced bill-and-keep incorporates an unreasonable and arbitrary misallocation of common costs. Sprint's Comments claim that bill and keep eliminates arbitrary "allocation of common costs". However, even Sprint admits that bill and keep "does not eliminate the need to allocate common costs across services.'' In fact, bill and keep results in common cost allocations that are arbitrary, unreasonable, unsupported, and unjustified. For example, Atkinson-Barnekov acknowledges that interconnection services would utilize the switch.

But for no valid reason, Atkinson-Barnekov proposes that zero percent of the "common costs" of the switch should be recovered from those interconnection services. This is an arbitrary and unreasonable allocation. Recovering no portion of the "common costs" of the switch from the interconnection services that use that switch would require that 100% of those switch "common costs" be recovered from other services that also utilize that switch. Since some of the other services would be "universal services," an over-allocation of common costs to universal services would be in violation of Section 254(k) of TA96, which requires that only a "reasonable" allocation of joint and common costs can be made to the universal services. Unbalanced bill-and-keep means the rates for the "surplus" traffic is zero. This means that traffic would be recovering none of the joint and common costs, although it would be benefiting from those costs.

X. Recommendation

A. We recommend that the Commission reject any mandatory unbalanced bill-and-keep. Under any unbalanced bill-and-keep, the effective price for the surplus traffic is zero. That zero price must be subsidized by charging higher rates to other customers, and that zero price attracts arbitrage. The zero price for this traffic does not reflect the economic cost of this traffic, and is economically inefficient. For these and the other reasons presented in our Comments, any mandatory unbalanced bill-and-keep proposal must be rejected.

B. It is hard to imagine a weaker argument for imposing an additional surcharge on end users, than the arguments that have been presented in favor of unbalanced bill-and-keep.

I. BILL-AND-KEEP WOULD DESTROY THE INTERNET FOR THE GENERAL PUBLIC.

A. The Proposal To Charge For Receivinp Calls Would Greatly Increase ISP's Costs, Which Would Be Passed On To Internet End-Users

America Online (AOL), one of the ISPs that has been instrumental in the development of the Internet, clearly indicates that ISPs will seek to recover from end-users the increase in costs that a bill-and-keep price structure would impose on the ISPs. AOL's Comments state:

> [I]f regulatory changes require CLECs to bear substantially greater transport costs to deliver the same services to ISPs they offer today, these rate increases will certainly pass to ISPs. In turn, ISPs will seek to recover cost increases through their rates to consumers. (emphasis added) (AOL Comments, p. ***6)***

Clearly, price increases for Internet services will harm the demand for those services. AOL recognizes this problem in its Comments when it states:

> Not only would a policy singling out Internet traffic arbitrarily and needlessly complicate an already complex issue, such a step could also have negative consequences for Internet traffic and usage, interfering with economically efficient price signals generally and dampening demand. (emphasis added) (AOL Comments, p. 4)

Both Staff proposals discuss at length the problem that the Internet has caused the FCC and the FCC Staff. (Paragraphs 83-85, Atkinson-Barnekov; Paragraphs 81-83, DeGraba) The FCC Staff proposes to deal with these problems by killing the Internet for the general public. They propose to kill the Internet by charging to receive calls. Since Internet Service Providers (ISPs) receive huge volumes of calls (while originating little or no traffic), this proposal will drastically increase the cost to the ISPs, and basically destroy

the Internet as a service that can economically be provided to the general public. The ISPs are the gateways through which the general public connects to the Internet.

B. SBC's and Similar Proposals Would Destroy the Internet

As is the case with both the DeGraba and Atkinson-Barnekov proposals, SBC's proposal would bill ISPs and others for receiving traffic. (See SBC Comments, Attachment ***2,*** Figure 1a) Therefore, the SBC proposal would destroy or seriously harm the Internet in the same way that either of the Staff proposals would. Others similar proposals, such as Qwest's or BellSouth's, would likewise destroy or harm the Internet.

C. Destroying the Internet for the general public is not in the public interest.

We understand the Internet has caused some regulatory problems for the FCC Staff. However, pricing the general public off of the Internet is not in the public interest. Placing additional "receiving traffic'' charges on the ISPs, and thereby harming the Internet is not in the public interest. In fact, the Telecommunications Act of 1996 (TA96) establishes the promotion of the Internet as part of the "policy of the United States." Section 230(b) of TA96 states,

> POLICY.--It is the policy of the United States--
> (1) to promote the continued development of the Internet and other interactive computer services and other interactive media;
> (2) to preserve the vibrant and competitive free market that presently exists for the Internet and other interactive computer services, unfettered by Federal or State regulation;

It has also been one of the FCC's stated goals to facilitate Internet growth.[1] Of course, both of the Staff proposals, as well as SBC's and similar proposals, are clearly designed to "fetter" the ISPs by imposing a huge new charge on them for "receiving" traffic.

Disrupting the "still-evolving information services industry" will directly hinder the goals of the 1996 Act to "preserve the vibrant and competitive free market that presently exists for the Internet".

II. BILL-AND-KEEP WOULD HARM AFFORDABILITY AND UNIVERSAL SERVICE

A. Sprint and NECA State that Bill-and-Keel, Where Traffic is Out-of-Balance Would Dramatically Increase End Users' Rates

If a bill-and-keep structure is adopted where traffic is out-of-balance, the result will be dramatic increases in end user rates. For example, Sprint estimates that a move to a bill-and-keep rate structure will result in an increase between **$4.00** and $5.00 per line per month for end-users of Tier 1 LECs.[2] (Sprint Comments, p. **24)**

The impact on end users served by the smaller LECs would be even more dramatic. NECA states that the LECs in the NECA Common Line Pool would have to raise end user rates by an average of about $20 per line per month if the FCC implements a bill-

[1] In the Access Charge Reform Order, **FCC** 97-158, released May 16, 1997 paragraph **334.**
[2] At page 23 of Sprint's Comments, Sprint recommends that any transition from an access charge rate structure to bill-and-keep be implemented in both the federal and state jurisdictions simultaneously. However, it is not clear if Sprint's estimated rate impacts of a transition to bill-and-keep are based on the assumption that both federal and state jurisdictions make that transition.

and-keep price structure in the interstate and intrastate jurisdictions. NECA points out that the end user impacts are even more dramatic for smaller and more rural companies. NECA estimates that the end-user impact of these bill-and-keep proposals would be rate increases between $46 and $69 per month for those LECs with less than 1,000 lines. (NECA Comments, pp. 5-6)

Proponents of bill-and-keep clearly admit that a bill-and-keep price structure will result in the "inevitable consequence" of increasing end-users' rates. For example, Qwest's Comments state:

> The Commission should also refine existing universal service mechanisms to accommodate what, under 47 U.S.C §254(g), would be one of the inevitable consequences of bill-and-keep: an increase in total telecommunications rates for end users in high cost areas. (Qwest Comments, p. iii)

The DeGraba proposal alleged that bill-and-keep would only result in "slightly" higher charges to customers in high cost areas than in urban areas. (Paragraph 125, DeGraba)

The assumption that bill-and-keep would result in only "slightly" higher rates can now be laid to rest. It is not reasonable to describe a $4.00 to $5.00 per line, per month increase for Tier 1 LECs' customers and a $20.00 per line, per month increase for the NECA LECs' customers (and yet higher for small rural LECs) as a "slight" increase. The fact of the matter is that bill-and-keep would result in enormous end-user rate increases that would pose a devastating threat to the affordability of universal service for all consumers in both low and high cost areas.

B. NARUC is Correct That These Proposals Would Increase Rates Overall.

In addition, NARUC points out the IXCs' historical track record of failing to pass through the benefit of access charge reductions to end-users. NARUC indicates that a failure to pass through access charge reductions to end-users under bill-and-keep would result in a rate increase on all consumers. NARUC's Comments state:

> Under bill and keep, carrier-to-carrier fees would be substantially reduced and in some cases eliminated. Instead the end user customers would pay many of those fees - probably via a new monthly fee to recover a substantial portion of the costs of access to and from their homes. Long distance companies' costs would be reduced as their access costs would, to a great extent, be shifted to end-users. If, as history suggests, long distance companies fail to pass on the savings or only pass them on to select customers, then it is possible bill and keep would lead to a rate increase to all consumers or to a significant portion of them. Indeed, under a unified bill-and-keep regime, consumers would pay a substantial part of the access costs for terminating a call at their home, even if it were a call they did not wish to receive. (emphasis added) (NARUC Comments, p. 5)

C. NARUC and State Commissions Recognize That These Proposals Would Make Service Unaffordable For Many Local Customers

State Commissions recognize the adverse impacts these proposals will have on the affordability of telephone services. For example, NARUC recognizes these proposals would make telephone service unaffordable for many customers. NARUC's Comments state:

> In high costs States, local customers may not be able to afford the increase in monthly fees possible under the FCC's bill and keep proposals. This could put upward pressure on State and federal universal service funds to provide funds to keep subscribers on the network. (NARUC Comments, p. 4)

The Florida Public Service Commission's (FPSC) Comments state:

> While the FPSC does not have specific estimates, it is conceivable that in high-cost states, local customers may not be able to afford the increase in monthly fees possible under the various bill-and-keep proposals. (FPSC Comments, p. **3)**

D. CompTel is Correct That Bill-And-Keep Would Eliminate A Consumers' Abilitv To Limit Toll Calling In An Effort To Keep Telephone Rates Affordable

Since the proposals presented in this proceeding would shift traffic sensitive costs directly to end-users in the form of mandatory flat rates, consumers will no longer be able to keep telephone bills affordable by limiting their toll calling. CompTel recognizes this fact in its Comments. CompTel's Comments state:

> In a very real way, the mandatory bill-and-keep proposals upon which the Commission has requested comment would wrest control over telecommunications costs away from subscribers, because they would no longer be able to reduce costs by choosing to place fewer calls. (CompTel Comments, p. iii)

III. FORCING CUSTOMERS TO SUBSIDIZE THE "FREE" SERVICE PROVIDED TO CARRIERS. IS NOT IN THE PUBLIC INTEREST

CompTel's Comments state:

> [W]here the traffic flow between competing carriers is not roughly equal, mandatory bill-and-keep effectively sets an intercarrier compensation rate of zero for the surplus traffic. An intercarrier compensation rate of zero is not cost-based, and thus violates the Telecommunications Act of **1996,** the U.S. Constitution, and the Reference Paper on Pro-Competitive Regulatory Principles negotiated as part of the WTO Basic Telecom Agreement. (CompTel Comments, pp. i-ii)

One of the reasons that end user rates would increase under this proposal **is** that the end users would have to subsidize "rate of zero for the surplus traffic." Customers that are considered "end users'' would have to pay higher rates because customers that are

considered "carriers" would be receiving free service under the DeGraba, Atkinson-Barnekov, SBC, and similar proposals. As stated in Paragraph 12 of the DeGraba proposal, current bill and keep arrangements are generally accepted only if "traffic is relatively balanced." The "balance" requirement means that the originating carriers are making a "payment in kind" for the terminating services they have received.

However, the DeGraba, Atkinson-Barnekov, SBC, and similar proposals involve simply providing free service to other carriers, with no requirement that those other carriers pay for those services either using money or by providing an equivalent amount of offsetting service in "payment in kind." Instead, those free services to customers who are considered "carriers" would simply have to be subsidized by customers who are considered "end users," which requires implicit subsidies.

Worldcom also recognized that the proposed rate structure would require subsidization, unless the Commission tried to pretend that the traffic sensitive costs were not traffic sensitive,

> However, the Commission cannot mandate the adoption of any bill-and-keep mechanism for significantly out-of-balance traffic unless it finds that the cost of switching is usage insensitive.'' (Worldcom Comments, page **20)**

Of course, many switching and transport costs are traffic sensitive. (More equipment is required to handle a higher level of traffic.) Therefore, charging zero for the "out-of-balance" traffic sensitive costs requires subsidization.

IV. FORCING LOW USE CUSTOMERS TO SUBSIDIZE HIGH USE CUSTOMERS IS NOT IN THE PUBLIC INTEREST

Another major reason that the average end user rates would be higher is because their rates would be increased in order to subsidize the usage costs of the high volume users. These proposals generally propose that certain traffic sensitive costs be billed to the end users as a flat rate fee. The same flat rate would be charged to high volume and low volume users. That flat rate would have to reflect some "average" level of usage. Therefore, the high use customers would be paying them the traffic sensitive costs that they are causing, and the low use customers would be paying more than the traffic sensitive costs that they caused. Quite simply, the low use customers would be forced to subsidize the high use customers. This is not in the customers' interest as CompTel's Comments state:

> Imposition of a mandatory bill-and-keep regime where the traffic flow between competing carriers is not roughly balanced would also be anti-consumer. For example, if subscribers were charged on a per call or per minute of use basis, they would be able to avoid additional charges only by refusing to answer their phones and refusing to use answering machines. The result would be even worse where subscribers are charged on a flat rate basis because they would have no means whatsoever to avoid the additional costs they would incur for receiving calls. It is hard to imagine that the public interest would be served by forcing families to pay higher costs for calls from telemarketers or political pollsters that interrupt their dinner based on the false assumption that these calls benefit the families as much as the telemarketers and political pollsters, particularly when the families may not have the means to avoid these additional costs. (emphasis added, CompTel Comments, p. iii)

AT&T also correctly indicates that these proposals would "subsidize unwanted calls." (AT&T Comments, page 25) Of course, the proponents of these proposals prefer a fixed flat rate charge, in part because that helps hide the impropriety of these charges from the public. Can you imagine the outcry if customers actually received bills that specifically listed that they were being charged for receiving telemarketing calls that interrupted their

dinner, and which they had no wish whatsoever to receive? The proponents of these proposals have no desire to be honest with the customers. Therefore, they propose disguising what is being charged for through mechanisms such as a fixed flat rate charge where the actual charges per unwanted call are not displayed.

A. Subsidizing Service Will Tend to Stimulate the Subsidized Service

AT&T properly recognizes that bill-and-keep will promote an increase in unwanted calls. AT&T's Comments state:

> When a telemarketer calls during the middle of dinner or a bath, for example, the harm to the called party, who would strongly prefer not to be interrupted, can be quite large. More generally, a called party may not want to receive a call because of the identity of the caller, the subject matter of the call, or the time that the call is placed. An efficient compensation rule would seek to minimize this over-utilization of the network by requiring the calling party, to the greatest extent possible, to bear the costs caused by the call, B&K would do just the opposite. By shifting some share of the direct costs of every call to the called party (and effectively allowing the calling party to terminate calls for free), B&K would encourage *more* unwanted calls. (AT&T Comments, p. *25)*

AT&T raises an important point. When the price presented to a telemarketer does not reflect the full cost (which is what would occur under the DeGraba, Atkinson-Barnekov, SBC or similar proposals), then the telemarketer would make calls where the benefit even to the telemarketer is less than the actual cost of the calls. This inefficient result would stem directly from changing from a CPNP structure to a bill-and-keep price structure. Of course, such increased subsidized traffic will require a greater subsidization from the end users.

B. Providing Free Service To Carriers Is Not One Of The "Protected" Universal Services, and Therefore Universal Service Funds (USFs) Cannot Be Used For That Purpose

As previously discussed, virtually all of the parties recognize that the bill-and-keep proposals would result in increased rates. Some parties have suggested that adjustments would have to be made to USFs as a result. (Qwest Comments, page iii; NARUC Comments, page 4) However, the primary purpose of these higher rates would be to subsidize free service for carriers where traffic is unbalanced. Subsidizing carrier traffic is not one of the "protected" universal services, and therefore, utilizing USFs for this purpose would be in violation of Section 254(c) of TA96. Another reason for the higher rates would be to force the low use customers to subsidize the high toll-use customers. Toll usage from high use customers is not one of the "protected" universal services. Therefore, the use of the USFs to support this purpose would be in violation of Section 254(c) of TA96.

V. BILL-AND-KEEP FOR UNBALANCED TRAFFIC WOULD CREATE NEW OPPORTUNITIES FOR ARBITRAGE.

Verizon's Comments correctly state:

> Any bill-and-keep system could provide opportunities for gaming. In particular, if "carriers" did not have to pay for certain types of transport, while "end users" did, it would cause some end users to try to masquerade as carriers to try to get the benefit of the better deal. (Verizon Comments, p. 19)

Discriminatory treatment based upon the classification of a customer creates arbitrage. Giving a service away free to certain classes of customers, while charging other classes of customers for otherwise similar service, causes any prudent customer to try to move

from the class of customers that is paying the subsidy, to the class of customers that is receiving the subsidized service.

All of the bill-and-keep proposals presented would provide certain services free to customer that are considered "carriers," while forcing the customers who are considered "end users" to support the full cost of those services and facilities. For example, under either the DeGraba and Atkinson-Barnekov proposals, if a customer is considered a "carrier," that customer would use the LEC's local switching equipment for both incoming and outgoing traffic at no charge whatsoever. However, customers that are considered "end user" customers of the LEC would have to pay for all of the local switching costs of the LEC. Therefore, a customer would continue to use the LEC's local switch, but cease paying for the use of that local switch if they changed their identification from being an "end user" customer to being a "carrier" customer. Likewise, as discussed in our Initial Comments, if a customer is considered an "end user" customer, that customer has to pay for all of the loops going between that customer premise and the LEC. However, if that customer becomes a "carrier" customer, then that customer must only pay for their half of the cost of what used to be considered the loops, or pay for only those loops that are carrying traffic in one direction. This is discussed in more detail in our Initial Comments. (See Attachment A to our Initial Comments.)

The other related proposals presented in the Initial Comments, including the proposal of SBC, also provide certain services free to customers that are considered "carriers", but charge for those same services if the customers are considered "end users."

A. Cost-Based Rates Are the Solution To The Arbitrage Problems, Not Free Service to Some as Occurs Under Out-of-Balance Bill-And-Keep

AT&T's Comments state:

> The Commission identifies two phenomena under the existing system that it labels "regulatory arbitrage". First, the Commission argues that the rates for reciprocal compensation may be "inefficiently structured or set too high" in ways that have created inefficient incentives for new entrants to target customers with predominantly terminating traffic. Second, the Notice contends that the **ESP** exemption gives providers of IP telephony an "artificial cost advantage" over interexchange carriers. To the extent that regulatory arbitrage opportunities exist today, they are the direct result of rates that strav significantly from economic costs. (citations omitted, emphasis added) (AT&T Comments, p, 14)

Since the problem of regulatory arbitrage stems directly from inappropriate rate levels, the answer to the problem of arbitrage is to simply ensure that rate levels are appropriate.

Under the existing price structure, some ISPs moved to a "carrier" classification in order to take advantage of an opportunity to charge other carriers very high terminating access charges. However, arbitrage incentives will also arise when a price structure presents the opportunity for certain classes of customers to obtain valuable services for free. This new arbitrage incentive would result under a bill-and-keep price structure, if there is no traffic balance requirement. Under bill-and-keep (with no balance requirement), a customer can obtain free service by simply changing their classification from "end-user" to "carrier" (or working with an existing "carrier"), as discussed above and on Attachment **A** to our Initial Comments.

AT&T properly recognizes that bill-and-keep will merely substitute carriers' incentive to arbitrage by gaining customers who primarily terminate calls, with an incentive to arbitrage by gaining customers who primarily originate calls. (AT&T Comments, p. 30) Bill-and-keep (with no traffic balance requirement) will create an arbitrage opportunity to charge unreasonably high rates is substituted for an arbitrage opportunity to receive valuable services for free.

B. The Incentives For Bill and Keep Are Enormous

The incentives for arbitrage under bill-and-keep (with no traffic balance requirement) are simply enormous. For example, if a large business that has a PBX switch classifies itself as an "end user," they must pay the LEC's for using the LEC's local switch for incoming and outgoing traffic. However, if the business works with a carrier or classifies itself as a carrier, this customer would avoid all the LEC local switching charges, and instead receive use of the LEC switch for free for both incoming and outgoing traffic. (See Attachment **A** to our "Initial Comments.") Obviously, the opportunity to receive free service simply by changing your classification from an "end-user" to a "carrier" represents an incredible incentive to arbitrage.

C. SBC'S Proposal Would Result In Arbitrage

SBC, Qwest, and BellSouth claim that bill-and-keep will prevent regulatory "arbitrage". (SBC Comments, p. 49; Qwest Comments, p. 15; BellSouth Comments, p. 12) However, Qwest and BellSouth generally supported some form of the DeGraba and Atkinson-

Barnekov proposals, which do create the incentive for arbitrage. (Both proposals give free service to customers that are considered "carriers," whereas customers that are considered "end users" pay for services.) Likewise, the SBC proposal would create similar massive arbitrage incentives.

Under SBC's proposal, by converting from an "end user" to a "carrier" classification, (1) the customer would change from paying for both the "incoming" and "outgoing" usage costs of the LEC's switch to receiving free usage of the LEC's switch for incoming traffic; and (2) the customer would change from having to pay for all the loops carrying traffic to and from their premise, to paying for only the cost of the facilities used to carry traffic from their location to the LEC. The facilities used to carry traffic from the LEC to them would be free if that customer is considered a "carrier."

In plain English, this means customers that are considered to be carriers have unlimited use of certain LEC facilities absolutely for free. Under the SBC proposal, "carriers" would be granted unlimited free use of both the "loops" (or equivalent facility) and the LEC's central office switches for unlimited amounts of incoming traffic.

However, under the **SBC** proposal, as an "end user", this same customer with the same traffic would be responsible for paying the traffic sensitive local switching costs associated with both incoming and outgoing traffic, and paying for all loops to and from them.[3]

[3] **An** "end user" would pay basic rates and the end user common line (EUCL) charge plus the new proposed bill-and-keep flat rate charges on all loops that connect traffic to or from the their premises.

It would not be necessary for a customer to actually become a "carrier"; instead, they could simply work out cooperative arrangements with an existing carrier to gain arbitrage advantages from the "free" service that is provided carriers under DeGraba and Atkinson-Barnekov, and SBC.

VI. UNBALANCED BILL-AND-KEEP WOULD NOT ELIMINATE "IMPLICIT SUBSIDIES": IT WOULD CREATE NEW ONES

SBC's Comments stress at length the importance of eliminating "implicit subsidies". For example, SBC's Comments state:

> First, prior to implementing bill and keep, the Commission and the states must ensure that implicit subsidies are eliminated and replaced with explicit recovery. (SBC Comments, p. 3)

However, the irony of SBC's statement, is that bill and keep, (where the traffic is not balanced), is an implicit subsidy. Since the "carrier" customer would receive free unlimited use of the LEC's switching equipment, those local switch costs would be paid for by the customers that are considered to be "end user" customers. The "end user" customers would have to subsidize the "carrier" customers' use of the LEC's local switch. Under DeGraba and Atkinson-Barnekov proposals, both "carrier" and "end user" customers would place traffic through the LEC's switches. However, only those customers that are classified as "end users" would be paying for those LEC switches, whereas the customers that were using the switches but were classified as "carriers," would not be paying for those switches.[4]

[4] Under SBC's proposal, the "end user" customers would be paying for the use of the local switches for both incoming and outgoing traffic, whereas the "carrier" customers would be paying for the use of the local switches for outgoing traffic, but would receive free use of the local switches for incoming traffic.

For outside plant, the "carrier" would also only pay a portion of the cost of the facilities between its itself and the LEC's central office. The remaining portion of the cost of those facilities would also have to be covered by the "naïve" customers who had not learned how to arbitrage SBC's proposal, and were still considered "end user" customers. Since the carrier customers are receiving use of some of the LEC facilities at no charge whatsoever, the cost of those facilities would have to be subsidized by the "end user" customers. Of course, as more and more customers learn how to arbitrage this proposal, the number of customers actually contributing to the cost of the LEC's switching equipment (and paying all of their loop costs) would decline, and therefore the cost per naïve customer would have to increase until a breaking point was reached. (See Attachment **A** attached to our Initial Comments for more details.)

VII. CALLED CUSTOMERS DO NOT KNOW THE VALUE OF THE INCOMING CALL. THEREFORE, THEY CANNOT MAKE ECONOMICALLY EFFICIENT DECISIONS

A. A Called Party Is Not In A Position To Assess The Efficiency Of Accepting A Call

The Allegiance Telecom's Comments on page 21 state:

> Requiring the recipient of mail to pay one-half the postage is the postal equivalent of the COBAK and BASIC proposals—it makes no sense.

Requiring customers to pay for receiving unwanted telemarketing calls is exactly the same as requiring them to pay for receiving unwanted junk mail. It makes no sense. The party that controls whether these costs are incurred is the party that sends the call or junk

mail, not the party that receives them. Qwest argues that it is acceptable to charge customers to receive calls because the called party "chooses whether to accept the call". Qwest's Comments state:

> In any call, both the calling party and the called party make choices that result in the accrual of costs. **A** calling party chooses to place a call and, at every moment during the call, chooses whether to allow it to continue. The called party chooses whether to accept the call and also chooses, at each point after the first moment, whether to maintain the connection. (Qwest Comments, p. 20)

First of all, the proponents of bill-and-keep generally support the imposition of a flat rate charge on end users to pay for the traffic sensitive costs of receiving calls. (NPRM, Paragraph **28)** Therefore, the customers would be charged a "flat rate" for "receiving" calls, regardless of whether a specific customer chose to answer or not answer their telephone. **A** flat "receive" charge to cover traffic sensitive costs is not reflective of the number of calls that a specific customer answered. In addition, the originating customer is the only customer that is in the position to make the efficient decision. The originating customer knows what the content of the call will be, and therefore knows the benefit of the call. If that customer is also presented with a price that properly reflects the cost of the call, then the originating customer has the information to make an economically efficient decision. The current practice of having the originating customer pay for the call results in efficient decision making.

However, under a bill-and-keep structure, such as those proposed by the DeGraba, Atkinson-Barnekov, and SBC in this proceeding, the customer that receives the call would be forced to decide whether to receive the call or not. That customer would be

presented with a price; however, they would not know the content, and therefore the benefit, of the call. Since they do not know the benefit, they are not in the position to make an economically efficient decision.

B. Unwanted Calls Result In Great Inefficiency Even If the Called Party Quickly Hangs Up: The Significant "Setup" Cost Would Already Have Been Incurred

Qwest argues that bill-and-keep is efficient because "it gives called parties appropriate incentives to end calls earlier if their continuation would be inefficient". (Qwest Comments, p. 21) However, one problem with Qwest's argument is that even if a customer hangs up very quickly once they realized that "continuation would be inefficient", a major portion of the traffic sensitive cost of the call has already been incurred to "setup" the call. Equipment is required to set up a call that is not required to continue the call.[5] The cost to "setup" a call, which is one of the most expensive traffic sensitive parts of a call, is incurred regardless of whether the call lasts ten seconds or ten minutes. As Qwest acknowledged in its Comments, "the terminating carrier typically has no control over whether it incurs call set-up costs". (Qwest Comments, p. 20)

In addition, the bill-and-keep proponents generally propose that the "receive" charge be a flat rate charge. Therefore, billing to the customers would not be based upon whether or not that particular customer chose to terminate calls earlier. (Of course, the proponents of these proposals do not want the receiving charge to be separately billed for each call,

[5] For example, from the digits dialed one must identify where the call should be sent, and must identify a route where the switching equipment and interoffice facilities to connect the call. In addition, data for

because that would inform the public of the absurdity of what they were being charged for. The public would not stand for receiving a bill that shows they were being charged for receiving a telemarketing call that they had no desire to receive.)

C. Charging Customers to Receive Calls Would Have the Same Result that Exists in the Cellular Industry-There are No Phone Books

Sprint argues that by making his or her telephone number available in the white pages directory, a customer is indicating a willingness to receive telephone calls. Sprint argues this demonstrates that called party plays a role in causing the cost of a call. (Sprint Comments, p. 15) Sprint's argument is flawed for several reasons. First of all, customers do not place their names in the white pages, the LEC does. If a customer does not want their name in the phone **book,** the customer has to pay the LEC monthly "non-published" rates to prevent the LEC from publishing their name and telephone number. In short, this proposal amounts to the customer either having to pay the LECs to not have their telephone number published, or they would have to pay extra charges for receiving calls that they do not want. Either way, the customer is charged extra for something they do not want. This proposal clearly does not treat the consumer fairly.

If customers were to be charged for incoming calls, there would likely be very few numbers listed in the white pages directory.

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billing must be recorded. Information pertaining to the calling number for Caller ID, Call Return, or Call Trace purposes must be identified retained, and processed, etc.

In fact, this is exactly what has happened in the cellular telephone industry. There are virtually no cellular telephone books. The reason for this is that that cellular customers generally must pay for receiving calls. Therefore, most cellular customers do not want their cellular phone number made available to the public. If wireline customers were forced to pay to receive calls, then it is reasonable to expect that the wireline telephone books would either disappear or have greatly reduced listings. Likewise, many customers would not want their telephone numbers published in any Internet telephone directories, or available from the operators. Forcing customers to pay to receive many calls would result in more unlisted numbers, and would greatly reduce the usefulness of the nationwide network as a public network.

D. Bill-And-Keep Would Result In Customers Paying for Unwanted Calls

CompTel recognizes that bill-and-keep would create the perverse result of customers being forced to pay for unwanted calls. CompTel's Comments state:

> For example, if subscribers were charged on a per call or per minute of use basis, they would be able to avoid additional charges only by refusing to answer their phones and refusing to use answering machines. The result would be even worse where subscribers are charged on a flat rate basis because they would have no means whatsoever to avoid the additional costs they would incur for receiving calls. (CompTel Comments, p. iii)

CompTel's Comments regarding customers refusing to answer their phones and answering machines is supported by what has happened in the cellular industry. Since cellular customers are generally charged to receive calls, many cellular customers turn their phones off when not placing calls, in order to avoid receiving (and therefore being

forced to pay for), unwanted calls. Because of this, four times as many calls are placed from cellular phones than are received by cellular phones.

> That ends up discouraging them from giving out their wireless phone number. … the typical profile for U.S. cellular usage is about 80% outbound calls, 20% inbound,… (Page ***37,*** America's Network, "The Keys to PCS Profitability", April 1, 1997)

If wireline service is to be priced with a customer paying to receive the calls, then the wireline customers will also be reluctant to receive calls. **As** a result, most calls simply would not go through because the receiving party would have their phones and answering machines turned off to avoid having to pay unwanted charges. This would make it more difficult to communicate, and would therefore seriously degrade the value of the network.

E. BILL-AND-KEEP WOULD NOT ELIMINATE MONOPOLY POWER.

AT&T correctly states that bill-and-keep will not limit LEC market power, but will rather simply shift the potential for monopoly abuse away from carriers and onto end users. AT&T's Comments state:

> Moreover, at least with respect to incumbent LECs, these terminating access monopolies exist - and will continue to exist - independent of the CPNP/B&K choice. This is because incumbent LECs will for the foreseeable future continue to retain substantial local market power over both end users and other carriers. Thus, absent regulation, these LECs could abuse their monopolies whether or not they were required to charge other carriers or end users for termination. See ***Ordover-Willig*** ¶54 ("incumbent LECs retain substantial market power, and thus, all that B&K would do is change the entity that must be protected from LEC market power"). In other words, limiting carriers' ability to abuse their market power as to other carriers would do nothing to alter their ability ultimately to abuse that market power as to end users. (AT&T Comments, p. 17)

AT&T is correct. The LECs' monopoly power would not be eliminated or significantly reduced by a bill-and-keep price structure. For most customers (especially residential customers), there is only one company that has a loop to the premise. The company that has that loop is the only company that can provide access service to and from the premises. That monopoly power will still exist regardless of whether the DeGraba, Atkinson-Barnekov, or some similar bill-and-keep proposal is adopted. The only difference is that currently it is the IXCs that must deal with the fact that this access service is essentially a monopoly service. The DeGraba and Atkinson-Barnekov proposals would shift the threat of monopoly abuse onto the end user. The monopoly power would not be eliminated, only the party paying the access charges to the monopoly service provider would change.

VIII. BILL-AND-KEEP WOULD REQUIRE MORE REGULATORY OVERSIGHT THAN THE CURRENT PRICE STRUCTURE, NOT LESS

A. Regulators Would Still Have To Regulate Access And Transport Rates - In Addition, They Would Have To Deal With A Number Of New Problems

SBC claims that it hopes its proposal "avoids the need for regulatory intervention". (SBC Comments, p. 30) However, this desired outcome would not result. As AT&T points out, the Commission would need to regulate charges for termination of calls under either CONP or B&K. AT&T also indicated that the potential for LECs to charge unreasonably high end-user rates for termination continues, and therefore the end-user rates would continue to need regulatory oversight. (AT&T Comments, p. 27) As

discussed in the prior section, the LECs would still have monopoly power. Therefore, the need for regulation to prevent the abuse of that monopoly power would continue.

As long as there is significant monopoly power, the fact that the access services would be billed to end users instead of billed to IXCs does not absolve the regulators from the responsibility of seeing that those charges for access services are reasonable. The end users are as deserving of protection from unreasonable access charges as are the IXCs. It would still be necessary for regulators to regulate both the transport rates and access charges, much as they do today.

Not only would the need to regulate the companies' monopoly power continue, but new regulatory burdens would be caused if any of these proposals are adopted. **As** CompTel accurately indicated in its Comments, bill-and-keep would increase the need for regulation:

> The imposition of mandatory bill-and-keep where the traffic flow between carriers is not roughly equal would also require the Commission to create problematic new regulatory distinctions (e.g. the definition of central office or local access) that determine which interconnecting carrier would bear the costs of transport and access, and thus which carrier would have to recover these costs from its end-users. This would require, among other things, stringent new regulation of transport services, and would spawn a whole new series of disputes between carriers with market power and their competitors. Implementation of these new regulatory distinctions, which have no real meaning in the context of the network, would be administratively burdensome, complex and expensive. Thus, imposition of mandatory bill-and-keep would not represent step towards deregulation, but rather the exchange of one regulatory scheme for another that would favor carriers with market power, and blunt the incentives that vigorous competition creates.

In addition, huge incentives for customers to move their traffic from being considered "end user" traffic to being "carrier" traffic would require constant regulation review and interpretation. Since the "carriers" would receive many services from the LECs for free, but "end users" would have to pay for those similar services (plus pay to subsidize the free carrier services), customers would want to move their traffic from being considered "end user" traffic to be considered "carrier" traffic. The regulators would have to make, enforce, and interpret complex definitions as to what customers are considered "carriers", and what customers are considered "end users." In addition, end users may make complex arrangements with existing carriers, whereby the end user traffic would become "carrier" traffic. The Commission would have to enter into arbitrary, complex, and continuing analyses in order to deal with the arbitrage incentive of the unbalanced bill-and-keep proposals.

IX. THE FRAGMENTATION OF RESPONSIBILITY FOR CALLS INHERENT IN BILL-AND-KEEP MAKES THE STRUCTURE UNWORKABLE

AT&T's Comments describe the customer's nightmarish task of having to add up the charges of three separate carriers' bills in an attempt to determine what they were paying for their long distance calls, due to the fragmented responsibility under a bill-and-keep price structure. AT&T's Comments state:

> B&K would cause additional radical changes to long distance pricing. Today, competing providers advertise, and consumers generally pay, a single price for long distance service. In a B&K world, consumers would have to add up the charges of three carriers - the originating LEC, the IXC, and the terminating LEC in order to determine what they are paying for long distance calls. (AT&T's Comments, **p.** 33)

The fact is that a bill-and-keep rate structure will necessarily fragment the responsibility for each call. As AT&T correctly points out, currently one company is responsible for each call from end-to-end. Qwest's Comments also highlight the difficulties surrounding assigning responsibility for transport under bill-and-keep. Qwest's Comments state:

> [T]he Commission should seek further comment before reaching any final decision on the most single important variable that separates the different proposed versions of bill-and-keep: the proper allocation of responsibility for transport. Although the DeGraba proposal discussed in the NPRM is a promising start, that proposal falters in proposing a "penalty default" that may be inefficient and would automatically require time consuming negotiations among carriers. (citation omitted) (Qwest Comments, p. 5)

However, under a bill-and-keep rate structure, no company would have end-to-end responsibility. For example, under the DeGraba proposal, for a long distance call, three different carriers would each have responsibility for different sections of the same call. (Paragraph 38, DeGraba)

The IXC would be responsible for the call only from the point of presence (POP) to the called party's central office. That is all it would be paid to do. It would have no responsibility for the call on either end. Likewise, the originating and terminating LECs would be responsible for only their segment of the call.

Likewise, the Atkinson-Barnekov proposal is based upon independent networks, each interconnecting only by splitting the cost of the interconnection facilities. Other than that, they would be totally independent. Therefore, under this proposal as well, no

company would have overall responsibility for the call which transverses more than one network.

Therefore, numerous "end-to-end" responsibility decisions that are now made by the IXC (or originating LEC for local calls) would have to be made by the FCC, other regulators, or end users.

CompTel's Comments state:

> The imposition of mandatory bill-and-keep where the traffic flow between carriers is not roughly equal would also create incentives for a carrier to reconfigure its network in order to maximize the costs that its competitors incur to terminate calls that its consumers originate and minimize the costs that it incurs to terminate calls from the customers of its competitors. This behavior would lead to inefficient network configurations, and would spawn an entirely new series of disputes over what costs the respective carriers must bear, particularly as networks and technologies evolve. (CompTel Comments, page ii)

Although SBC favors bill-and-keep, as SBC admits,

> Moreover, a flashcut transition to a bill and keep regime whereby ILECs would be responsible for transport from the calling party's end office to the IXC's POP could encourage inefficient interconnection arrangements, to the extent an IXC could consolidate and relocate its POPs only for originating traffic in order to minimize its own transport costs. (SBC Comments, p. **29)**

Currently, if the IXC uses an LEC's service, the IXC determines where it will hand off the call from the IXC facilities to the LEC facilities. Since the IXC is paying both the access charges billed by the LEC, and for its own interexchange facilities, the IXC can make the analysis of the proper hand off point based upon economic analysis. For example, in determining whether to have one POP or several POPs in a **LATA,** the IXC would consider whether the higher cost they paid to establish more POPs would be offset

by reduced access charges that they would pay to the LECs. However, under bill-and-keep proposals, the location of the POP would no longer be subject to such reasonable economic analysis, because no one company would be paying for all of the services. Instead, it would be to the IXC's advantage to minimize its costs, even if that increased the costs to the LECs. For example, the IXC might utilize only one POP in a LATA instead of several. Having only one POP would reduce the IXC's costs, and therefore allow the IXC to charge its customer less, thereby gaining a competitive advantage over other IXCs. Of course, having one POP in a LATA instead of several would increase the access costs of the originating LEC, since the originating LEC would have to transport the calls a longer average distance to reach that one POP. However, increasing the access cost of the LEC would no longer have any financial impact on the IXC, because under these two Staff proposals the IXC would no longer paying the access costs of the LECs. The LEC could properly complain that the IXC's selection of POP locations raised the LEC's cost. Since no company would have end-to-end responsibility, the regulators would have to step in and make these determinations.

A. It Would Be Impossible for an End User to Identify Which Carrier Was Responsible for [illegible] of Service P[illegible]

Finally, with no carrier having end-to-end responsibility for the quality of the call, it would be a virtually impossible task to determine which of the several carriers involved in the call was responsible for any service problem.

There is no practical way for the end user to determine which of the several carriers was responsible for the quality of service problem. The rates and regulation of customer premise equipment (CPE) could be separated from the rest of the network only because the CPE could be physically disconnected at the wall jack. Therefore, the customer could determine whether a quality of service problem occurred in the CPE or the rest of the network.

Likewise, inside wiring could be separated from the rest of the network for regulatory purposes only because the end user could disconnect their inside wiring from the rest of the network at the network interface device (NID) located on the side of their house. However, there is no way that an end user accessible disconnection jack can be installed at the POP or central office. Therefore, under bill-and-keep there would be no way for the end user to determine which of the several carriers involved in the call was responsible for the quality of service problem. These proposals are simply unworkable as far as identifying the responsibility for quality of service problems.

X. BILL AND KEEP WOULD NOT AVOID THE PROBLEM OF COMMON COST ALLOCATION ENTIRELY-INSTEAD IT WOULD UNREASONABLY ALLOCATE ZERO PERCENT OF COMMON COSTS TO SOME SERVICES, AND 100% TO THE REMAINING SERVICES.

Sprint's Comments claim that bill and keep offers the elimination of an arbitrary "allocation of common costs". (Sprint Comments, **p.** 5) However, Sprint's claim is false. **As** Sprint admits, bill and keep "does not eliminate the need to allocate common costs across services." (Sprint Comments, **p.** 7) In addition, bill and keep would result in

common cost allocations that are not only "arbitrary", but that are unreasonable, unsupported, and unjustified. For example, Footnote 57 of Atkinson-Barnekov acknowledges that interconnection services would utilize the switch. But for no valid reason, Atkinson-Barnekov proposes that zero percent of the "common costs" of the switch should be recovered from those interconnection services. Recovering no portion of the "common costs" of the switch from the interconnection services that use that switch would require that 100% of those switch "common costs" be recovered from other services that also utilize that switch. This is not only an "arbitrary" allocation, it is also an unfair, unreasonable, and unsupported allocation. The Atkinson-Barnekov proposal presents no reasonable justification for arbitrarily allocating 100% of the common costs to other services, and zero percent of the common costs to the interconnection services. Those switch common costs do have to be recovered. There is no reason that the interconnection services should not support a reasonable share of the common costs of the switching equipment which they, along with other services, utilize.

Likewise, the other common costs of the companies that provide switching or transport facilities are also costs that would have to be recovered. For example, these companies undoubtedly have executives, attorneys, accountants who prepare income tax returns, and similar common costs. However, under the bill-and-keep proposals, when traffic is unbalanced, the effective rate for the "surplus" traffic is zero. Therefore, that rate not only does not cover any of the incremental costs of that traffic, but also does not cover any of the common costs of the LECs. There is no valid reason that the interconnection

services provided by that company should be allocated zero percent of those common costs.

A. Section 254(k) Of TA96 Requires Reasonable Allocation Of Common Costs

Bill-and-keep would effectively allocate none of the common costs to interconnection services. That would have the effect of over-allocating common cost recovery to the remaining services. Since some of the other services would be "universal services," the over-allocation of common costs to universal services would be in violation of Section 254(k) of TA96. Section 254(k) requires that only a "reasonable" allocation of joint and common costs can be made to the universal services.

> Section 254(k)--SUBSIDY OF COMPETITIVE SERVICES PROHIBITED.--A telecommunications carrier may not use services that are not competitive to subsidize services that are subject to competition. The Commission, with respect to interstate services, and the States, with respect to intrastate services, shall establish any necessary cost allocation rules, accounting safeguards, and guidelines to ensure that services included in the definition of universal service bear no more than a reasonable share of the joint and common costs of facilities used to provide those services.

In fact, the "zero" common cost recovery that the Atkinson-Barnekov proposal proposes is not what occurs in competitive markets. Standard economic theory does not hold that prices in a competitive market will generally equal incremental cost. Instead, standard economic theory holds that prices in a competitive market will cover the total cost of an efficient firm, which includes both the incremental and common costs. If prices did not recover the common costs, even efficient firms would go bankrupt.

In fact, the FCC in its Interconnection Order found that prices should be based on the TELRIC of the service, plus a reasonable share of the joint and common costs. The FCC's Interconnection Order states:

> The Commission concludes that the prices that new entrants pay for interconnection and unbundled elements should be based on the local telephone companies Total Service Long Run Incremental Cost of a particular network element, which the Commission calls "Total Element Long-Run Incremental Cost" (TELRIC), plus a reasonable share of forward-looking joint and common costs.[6]

Utilizing bill-and-keep when the traffic is unbalanced, means the effective rate for the surplus traffic is zero. That does not cover either the incremental cost nor does it cover a "reasonable share of forward-looking joint and common costs."

XI. BELLSOUTH'S, QWEST'S, AND SBC'S PROPOSALS CONTAIN MANY OF THE SAME PROBLEMS

BellSouth and Qwest both recommend that the Commission move to a bill-and-keep system of intercarrier compensation. (BellSouth Comments, p. 29 and Qwest Comments, p. **48)** Qwest argues that the Staff DeGraba proposal is a "useful starting point", but that the Commission's should find a solution that will better minimize regulatory intervention, reduce the need for time-consuming negotiation, and "preserve appropriate incentives for the development of facilities-based competition in the provision of transport services". (Qwest Comments, p. 29) The BellSouth and Qwest proposals are essentially bill-and-keep proposals with no requirement that the traffic be balanced. Whatever refinements they propose are either minor or in general are poorly defined, and

would not correct this key problem. Any proposal which is bill-and-keep with no traffic balance requirement is charging a "zero" rate for the surplus traffic. That zero rate requires subsidization, and is an incentive for arbitrage. This fatal flaw cannot be corrected by minor "fine tuning." Therefore, our Initial Comments and these Reply Comments pertaining to the problems with the DeGraba and Atkinson-Barnekov proposals generally apply to modified versions of them, such as what might result from the BellSouth or Qwest proposals.

The SBC proposal is also very similar to the DeGraba proposal. For a long distance call, the primary difference between SBC's and DeGraba's proposals is that SBC appears to be proposing a different demarcation point between the LEC's and IXC's responsibility. Under SBC's proposal, the IXC would pay access charges to the LECs for transport between the originating LEC's end office and the IXC's POP, and the IXC would also pay the terminating LEC access charges for transport from the IXC's POP to the terminating LEC's end office. Other than that, the SBC proposal is similar to DeGraba's proposal. The customers that are considered "end users" would be fully responsible for all the LEC's local switching and loop costs, whereas the customers that are considered "carriers" would use those facilities for incoming traffic at no charge.

There would still be three carriers with independent responsibility for the call, and the end users would be billed by three different companies for each call. The difference between the DeGraba and SBC proposals is so minor that they do not

[6] Paragraph 29, FCC Interconnection Order, FCC 96-325

solve any of the problems discussed above. The SBC proposal would still mandate bill-and-keep between carriers for the use of the local switching equipment and loops to the customer premises, even if the traffic between carriers was unbalanced. (SBC Comments, Attachment ***2,*** Figure 2A) Therefore, the SBC proposal is unacceptable for the reasons that the unbalanced bill-and-keep proposals are unacceptable. Under unbalanced bill-and-keep, the rate for the surplus traffic is zero. **A** zero rate requires subsidization and attracts arbitrage.

A. SBC States That Bill-And-Keep Would Require The FCC To Revisit Many Major Decisions That The FCC Has Made in Recent Years

SBC's proposal would require the FCC to revisit many of the major telecommunications issues that the FCC has addressed in recent years. For starters, SBC would have the Commission initiate (a) a proceeding to "establish inducements for states to establish residential pricing structures that allow prices for residential local service to be set at levels that are self-supporting without reliance on implicit subsidies", (b) a proceeding to revisit the FCC's prices for unbundled network elements and discounted resale services and (c) a proceeding to conduct a "fundamental reexamination of universal service funding mechanisms". (SBC Comments, **pp. 21-22)** Also, SBC's proposal would somehow require that the intrastate rates adopt bill-and-keep. (SBC Comments, page 25)

In short, SBC is arguing that if bill-and-keep is adopted, many major decisions that the Commission has made in recent years would have to be discarded and redone.

B. SBC's Call For "Residential Local Teleahone Service Pricing Reform" is Unsupported and Misplaced

SBC argues:

> Prior to implementing a uniform bill and keep regime, the Commission must replace implicit subsidies with explicit recovery. This involves both residential local telephone service pricing reform and universal service support reform that establishes an affordability standard. (SBC Comments, p. 20) (emphasis added)

First of all, unbalanced bill-and-keep creates implicit subsidies. Under all of these proposals, the LECs would be forced to provide services and the use of facilities to carriers at no charge whatsoever for the "surplus" unbalanced traffic. That free service to carriers would have to be subsidized. Under all of these proposals, the low use customers would be forced to subsidize the high use customers.

Second, SBC provided absolutely no evidence that residential local telephone service is subsidized by any other services. (SBC Comments, page 2) The false allegation that residential local services are "subsidized" has been investigated, and generally flatly rejected by state commissions throughout the nation.

For example, the Washington Utilities and Transportation Commission (WUTC), in its Fifteenth Supplemental Order in Docket No. UT-950200 dated April 11, 1996, stated:

> The evidence clearly shows that residential service is covering its cost.

The Commission explained,

> The conclusion to be drawn from these cost results is that residential service does not receive a subsidy at current rates. The average residential customer today pays $10.50 for local service and **EAS** adders, plus a subscriber line charge of $3.50. If USWC were to exit the local residential

> exchange market, its revenues would decrease by $14.00 per customers, and its costs would decrease by about $4.42 per customer. Not only does residential service cover its incremental cost (the test for cross-subsidy), it even covers the incremental cost of the local loop that is used to provide local, long-distance, and vertical services, since the revenue from local service, including the subscriber line charge, exceeds the $13.38 cost of local service plus the local loop.[7]

Of course, the exact numbers vary from state to state, but the conclusion is the same. If the LECs ceased providing residential basic local exchange service, the lost revenue would greatly exceed the avoided cost. As the Washington Commission indicated, residential basic exchange service is priced greatly in excess of its incremental cost. Therefore, it is not receiving a subsidy, and in fact is producing a large contribution to joint and common costs.

In addition, the New Mexico Commission very recently reached a similar conclusion:

> The TSLRIC of a service necessarily requires inclusion of only those costs that would be eliminated if that one service were eliminated, while other services continued to be provided. Since the costs of the local loop would not be eliminated were local exchange service not provided, and all other services continued to be provided, the TSLRIC of local exchange service properly excludes the loop costs. (New Mexico Utility Case No. 3325, Order dated December 19,2000, **p.** 12)

> Staff based its decision to exclude the costs of the local loop and NTS COE from the TSLRIC for residential basic exchange service on the generally accepted economic principle that only those costs that are directly caused by the service are properly included in its TSLRIC. Thus, shared costs, i.e., costs of facilities shared by more than one service, are not properly included in the TSLRIC of one specific service. The Recommended Decision concluded that, inasmuch as the loop is a cost shared by a whole host of services - including, among others, basic exchange, toll, switched access, vertical services and high frequency data services - the cost of the loop is not directly attributable to basic exchange service. The Recommended Decision consequently found that <u>basic exchange service is</u>

[7] Page 90, Fifteenth Supplemental Order, Docket No. UT-950200, Commission Decision and Order Rejecting Tariff Revisions; Requiring Refiling, dated April 11, 1996.

making a contribution towards the shared costs of operating; a network, therefore, is not subsidized. (emphasis added) (Ibid, p. 8)

The New Mexico Commission specifically adopted the above Hearing Examiner's Recommended Decision in the above proceeding.

SBC provides no basis on which the FCC could properly find that residential basic exchange service is receiving a subsidy, other than the fact that it is to the company's advantage to claim this is true. The FCC has not conducted an investigation as to whether residential basic exchange service is or is not receiving a subsidy. The FCC has no reason to address this issue, since the FCC does not have jurisdiction over residential basic exchange rates. The regulatory agencies that do have jurisdiction over residential basic exchange service rates, the state commissions, have investigated these claims in the past, and have generally found that these industry claims were invalid, as the above quotations state. SBC's request that the FCC effectively overturn the regulatory determinations that are based upon analysis and inquiry by the state commissions (that have jurisdiction over local rates), is unfounded.

In addition, SBC's call for the FCC to implement bill-and-keep for intrastate access charges does not recognize the jurisdictional boundaries.

SBC also argues that "bill and keep must be implemented for interstate and intrastate switched access services at the same time". BellSouth argues that bill

and keep cannot operate for exchange access unless it is adopted in both the state and interstate jurisdictions. BellSouth's Comments state:

> Bill-and-keep could not work for exchange access if only one jurisdiction adopted it. **A** dichotomy of bill-and-keep in one jurisdiction and carrier access charges in another would simply invite regulatory arbitrage, with interexchange carriers being provided the precuniary incentive to mask the jurisdictional origin of the traffic that is assessed carrier access charges. (BellSouth's Comments, page **4,** Footnote **6)**

BellSouth argues that to ensure that all states adopt a bill-and-keep approach for intrastate access charges, the FCC can rely upon its general rulemaking authority to implement Section 251(a)'s duty imposed on all carriers to interconnect with each other. (BellSouth Comments, p. 26) However, regardless of what Section 251(g) says about carrier interconnection, it certainly does not give the FCC the regulatory authority to impose intrastate rates on end-users to subsidize free services to carriers.

What SBC and BellSouth effectively propose is to have the FCC attempt to interfere with the state commissions' jurisdiction over intrastate rates.

WorldCom's Comments properly state that the Commission does not have jurisdictional authority to reduce the intrastate switched access rates of carriers:

> An important limitation on the Commission's authority is its lack of jurisdiction over intrastate access charges...Since the Commission cannot itself order reductions in intrastate access charges, it will have to work with the state commissions to reduce these charges. (WorldCom's Comments, **p.** 17)

In addition, as SBC indicates in its Comments, many states have capped local service prices. (SBC Comments, p. 20) In many states, local service prices have been set as part of an alternative form of regulation (AFOR) price structure. In many cases, the LECs, including SBC, agreed to certain rates in return for other concessions. SBC is now asking the FCC to overturn the SBC agreed-to local rates (or impose an added intrastate charge, which is the same as a higher local rate). Some parties in this case are effectively calling for the FCC to supercede and revise the rates and regulatory structures that apply to intrastate rates that have been adopted by the respective state commissions.

Since the bill-and-keep proposal results in increasing customer rates to force low use customers to subsidize high toll-use customers, it would be improper for the FCC to force such a change in the intrastate jurisdiction, even if it had the ability to do so.

Since the unbalanced bill-and-keep proposals cause higher end user rates in order to force customers who are considered to be "end users" to subsidize free service provided to customers who are considered to be "carriers", such an arbitrary and arbitrage inducing change should not be forced upon the intrastate jurisdictions by the FCC, even if the FCC had jurisdiction to do so.

Since the unbalanced bill-and-keep proposals would not charge high volume users, such as telemarketers, rates that reflected the full economic costs that they caused, such rates are economically inefficient, and would stimulate inefficient use of the network. The

FCC should not impose such an improper rate structure on the intrastate jurisdiction, even if it had the jurisdiction to do so.

For all of these reasons, any parties' proposals regarding pricing reform for residential local service and other intrastate telephone services should be disregarded.

XII. CONCLUSION

The Maryland Office of the People's Counsel strongly recommends that the FCC reject bill-and-keep when traffic is unbalanced. When traffic is unbalanced, the price for the surplus traffic is zero. That zero price requires subsidization and invites arbitrage. The evidence presented by the parties (even including some proponents of bill-and-keep) clearly indicate that a bill-and-keep price structure will greatly increase the rates to end users, thereby harming the affordability of telephone services.

Recovering traffic sensitive costs in mandatory flat rates would require low use customers to subsidize high use customers.

Bill-and-keep, when traffic is unbalanced, would create undue discrimination in which customers considered to be "carriers" use certain LEC's facilities for free, whereas the customers considered to be "end users" would pay for those facilities. This would create arbitrage and require implicit subsidies.

The responsibility for each call would be fragmented, with several carriers having responsibility for different segments of the same call. No company would have overall responsibility for the call. Regulators would inherit the end-to-end responsibility.

By charging ISPs to "receive" traffic, these proposals would destroy the Internet for the general public. Charging customers to receive traffic would make many customers remove their telephone numbers from public directories, turn off their answering machines, and refuse to take calls.

Regulation of access and transport rates would still be needed, and monopoly power would still exist under these proposals. These proposals are economically inefficient. These proposals mis-allocate common costs by recovering none of the common costs from interconnection services. Unbalanced bill-and-keep proposals are simply "corporate welfare" proposals under which the carriers' "surplus" traffic is handled for free. We recommend that the unbalanced bill-and-keep proposals be rejected. They are just another name for requiring LECs to provide free service to certain favored customer classes.

CERTIFICATE OF SERVICE

I HEREBY CERTIFY that a copy of the Comments of the Maryland Office of People's Counsel will be furnished to parties on the attached list.

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